



920

Allowances

The President's budget and the Congressional budget resolution sometimes include amounts in function 920 to reflect proposals that are not clearly specified or that would affect multiple budget functions. Because the Congress actually appropriates money for specific pur-

poses, there are no budget authority or outlay totals for function 920 in historical data. In this volume, function 920 includes options that cut across programs and agencies and that affect multiple budget functions.

920-01—Discretionary

Raise the Threshold for Coverage Under the Davis-Bacon Act

(Millions of dollars)	2006	2007	2008	2009	2010	Total	
						2006-2010	2006-2015
Change in Spending							
Budget authority	-200	-200	-205	-210	-210	-1,025	-2,130
Outlays	-60	-150	-215	-255	-275	-955	-2,450

Since 1935, the Davis-Bacon Act has required that no less than “prevailing wages” be paid for all federally funded or federally assisted construction projects with contracts that total \$2,000 or more. The Department of Labor measures prevailing wages in a specific locality on the basis of the wages and benefits earned by at least 50 percent of workers in a particular type of job or on the basis of the average wages and benefits paid to workers for that type of job. Those procedures, as well as the classifications of workers who receive prevailing wages, sometimes favor union wage rates.

In recent years, proposals have been made that would raise the threshold for determining which projects are covered by the Davis-Bacon Act. This option would increase the threshold from \$2,000 to \$1 million. That change would save \$60 million in discretionary outlays in 2006 and \$955 million through 2010—provided that federal agencies’ appropriations were lowered to reflect the anticipated reduction in costs. (The higher threshold also would save less than \$5 million in mandatory spend-

ing in 2006 and about \$25 million over five years.) In addition, it would reduce the administrative burden on both firms and the government by restricting coverage to the largest contracts.

One rationale for raising the threshold is that it has remained the same for seven decades and raising it would allow the federal government to spend less on construction. Moreover, this option could increase the opportunities for employment that federal projects might offer less-skilled workers.

An argument against such a change is that it could lower the earnings of some construction workers. In addition, raising the threshold might jeopardize the quality of federally funded or federally assisted construction projects. The contention is that since firms are required to pay at least the prevailing local wage, firms covered by the Davis-Bacon Act are more likely to hire able workers, resulting in more timely completion of projects and fewer defects in the finished product.

920-02—Mandatory

Impose a Fee on the Investment Portfolios of Government-Sponsored Enterprises

(Millions of dollars)	2006	2007	2008	2009	2010	Total	
						2006-2010	2006-2015
Change in Receipts	+1,624	+1,656	+1,739	+1,826	+1,917	+8,762	+19,885

Government-sponsored enterprises (GSEs), private financial institutions chartered by the federal government, are intended to increase the availability of credit for specific purposes, such as housing and agriculture. They fulfill that role by raising funds in the capital markets on the strength of an implied federal guarantee and then lending (or otherwise conveying) monies to retail lenders. Investors who buy debt securities issued by the GSEs infer that those securities are federally guaranteed because of various provisions in the GSEs’ charters—such as provisions that exempt the enterprises from state and local income taxes, render their securities eligible to serve as collateral for federal and other public deposits, and authorize the Secretary of the Treasury to purchase those securities. That implicit federal guarantee, for which the government collects no fee, lowers the cost of borrowing for the GSEs and conveys a subsidy that gives the enterprises a competitive advantage in financial markets. Studies by the Congressional Budget Office and others have concluded that the GSEs receive substantial subsidies, a significant portion of which is not passed on to borrowers.

Four GSEs—Fannie Mae, Freddie Mac, Farmer Mac, and the Federal Home Loan Bank System—have used their special borrowing status to acquire and hold large portfolios of securities. Those investments consist mostly of mortgage-backed securities but also include other asset-backed securities, mortgages, corporate bonds, and mortgage revenue bonds. The investment portfolios of the four enterprises total about \$2 trillion, or about 75 percent of their combined assets, according to current reports. The GSEs earn profits from the difference in the yields they receive on their investments and the yields they pay on their subsidized debt issues. Those profits owe much to the federal guarantee.

This option would impose a fee of 10 basis points (10 cents per \$100 of investments) on the GSEs’ average daily investment portfolios. That fee would increase federal receipts by \$1.6 billion in 2006 and \$8.8 billion over five years. Proceeds from the fee would equal less than 20 percent of the total federal subsidy estimated to be retained by equity investors and other stakeholders of three housing GSEs (Fannie Mae, Freddie Mac, and the Federal Home Loan Banks).

A justification for imposing a fee on the GSEs’ investment portfolios is that it would promote competition in financial markets and recover some of the federal subsidy retained by those enterprises without reducing their capacity to achieve their public mission. For example, the fee would not restrict the authority of the housing GSEs to guarantee mortgage-backed securities or prevent them from purchasing those securities, nor would it hamper the ability of the Home Loan Banks to make advances to member banks. Because the fee would be a small fraction of the estimated subsidy retained by GSEs and their stakeholders, the GSEs might absorb it through lower profits and leave mortgage interest rates unchanged.

A disadvantage of imposing a portfolio fee is that investors might interpret it as a strengthening of the implicit federal guarantee, which could further weaken market discipline. Critics of this option might also argue that mortgage rates would rise in response to the fees because either the GSEs do not receive a government subsidy or they pass most of it on to targeted borrowers and hence should not be subject to a fee. Moreover, opponents might also contend that the fee would reduce the GSEs’ incentive to buy mortgage-backed securities during periods of financial stress, when the gap between interest rates on most securities and Treasury rates tends to widen.

RELATED OPTION: 370-02

RELATED CBO PUBLICATION: *Letter to the Honorable Richard C. Shelby regarding updated estimates of the subsidies to the housing GSEs*, April 8, 2004; *Testimony on Regulation of the Housing Government-Sponsored Enterprises*, October 23, 2003; *Effects of Repealing Fannie Mae’s and Freddie Mac’s SEC Exemptions*, May 2003; and *Federal Subsidies and the Housing GSEs*, May 2001

920-03—Discretionary**Eliminate Cargo Preference**

(Millions of dollars)	2006	2007	2008	2009	2010	Total	
						2006-2010	2006-2015
Change in Spending							
Budget authority	-356	-466	-581	-592	-603	-2,598	-5,798
Outlays	-299	-434	-549	-581	-596	-2,458	-5,633

The Cargo Preference Act of 1904 and other laws require that ships registered in the United States be used to carry certain government-owned or government-financed cargo that is shipped internationally. Traditional justifications for that “cargo preference” include maintaining the economic viability of the nation’s maritime industry and bolstering national security by ensuring that U.S.-flag vessels and U.S. crews are available during wartime.

Eliminating cargo preference would reduce federal transportation costs by allowing the government to ship its cargo at the lowest available rates. That change would save \$299 million in outlays in 2006 and a total of almost \$2.5 billion through 2010.

Two federal agencies, the Department of Defense (DoD) and the Department of Agriculture (USDA), account for most of the gross tonnage shipped under cargo-preference laws. The preference applies to nearly all of DoD’s freight and three-quarters of USDA’s shipments of food aid, as well as to shipments associated with programs of the Agency for International Development and the Export-Import Bank. Roughly 70 percent of the savings from eliminating cargo preference would come from defense discretionary spending, with the rest coming from non-defense discretionary spending.

One rationale for this option is that cargo preference represents a subsidy of private vessels by taxpayers, which

helps a handful of ship operators preserve their market share and market power. Another rationale is that cargo preference puts the U.S. government at a competitive disadvantage in selling surplus agricultural commodities abroad because it must pay higher costs to transport them.

A key argument against this option is that although DoD has invested in its own sealift fleet to transport military equipment and has contracted with foreign-flag ships when necessary, the department considers cargo preference an essential part of its sealift policy. Indeed, in deployments for the war in Iraq, DoD has made heavy use of U.S.-flag ships and has relied extensively on U.S. civilian mariners to crew its reserve ships. Another argument against this option is that cargo preference is necessary to offset federal requirements that raise labor costs and regulatory burdens and thus put the nation’s maritime industry at a competitive disadvantage. (Under federal law, U.S.-flag ships must be crewed by U.S. mariners and, in general, must be built by U.S. shipyards.) Without guaranteed business from cargo preference, many U.S.-flag vessels might leave the fleet—by reflagging in a foreign country to save money or by decommissioning altogether. In addition, U.S. ship operators and shipbuilders might default on loans guaranteed by the government. (The estimated savings shown above do not reflect the possibility of such defaults.)